

97-84053-19

Bledsoe, Samuel Thomas

Consolidation of railroads

[Santa Fe]

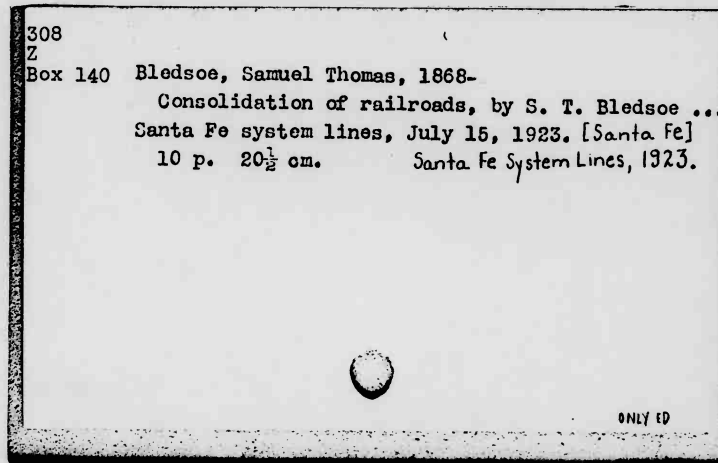
[1923]

97-84053-19
MASTER NEGATIVE #

COLUMBIA UNIVERSITY LIBRARIES
PRESERVATION DIVISION

BIBLIOGRAPHIC MICROFORM TARGET

ORIGINAL MATERIAL AS FILMED - EXISTING BIBLIOGRAPHIC RECORD



RESTRICTIONS ON USE: Reproductions may not be made without permission from Columbia University Libraries.

TECHNICAL MICROFORM DATA

FILM SIZE: 35mm

REDUCTION RATIO: 9:1

IMAGE PLACEMENT: IA (IIA) IB IIB

DATE FILMED: 3-26-97

INITIALS: ms

TRACKING # : 22835

FILMED BY PRESERVATION RESOURCES, BETHLEHEM, PA.

CONSOLIDATION OF RAILROADS

By

S. T. BLEDSOE
General Counsel

The Atchison, Topeka and Santa Fe
Railway Company

308

Z

Box 140

SANTA FE SYSTEM LINES

July 15th, 1923

CONSOLIDATION OF RAILROADS

BY S. T. BLEDSOE,

General Counsel, The Atchison, Topeka and Santa Fe
Railway Company

Prior to the effective date of the Transportation Act, February 28th, 1920, consolidation of operation and ownership of railroad properties had been controlled exclusively by the states, except insofar as Section 7 of the Clayton Anti-Trust Act, approved October 14, 1914, imposed limitations upon consolidations of interstate carriers. The laws and policies of the states were quite uniform in prohibiting the consolidation of either the control or ownership of carriers having parallel and competing lines, and sometimes parallel or competing lines. Some states by constitutional provision, legislative enactment, or both, prohibit the consolidation of the property of a railroad corporation organized under the laws of such states with those of a railroad corporation organized under the laws of the United States, or of any other state. Many states impose various limitations upon consolidations, and in addition thereto quite generally prohibit such consolidations except upon the approval of the public utilities commission of the state. There was no uniformity in the state requirements authorizing or permitting consolidations. If the property of a carrier was located in two or more states, it frequently found itself subject to conflicting state requirements, the state of incorporation claiming authority to control consolidations, as well as each state in which any part of its property was located. The difficulties were so great that consolidations of substantial carrier properties had in the majority of the states practically ceased.

The emergencies of the world war brought out the alarming effects of restrictions upon consolidations and upon co-operation between the carriers and of other re-

strictions imposed by Congressional regulation and state action, which rendered impossible the co-operation necessary to meet the emergency of winning the war. War transportation needs brought Congress for the first time to realize, to some extent at least, the effect of purely restrictive legislation in dealing with transportation questions.

In framing the Transportation Act of 1920, and particularly the provisions thereof relating to consolidation, it developed that the House and Senate had radically different views on the principles to be applied to consolidations. The Senate favored compulsory consolidation of the railroads of the United States into from twenty to thirty-five groups or systems, competition and channels of traffic to be preserved as fully as possible consistent with such consolidation.

The House favored authorizing voluntary consolidation along the lines of natural development of the country's transportation facilities, when in the public interest and subject to the approval of the Interstate Commerce Commission, competition and channels of traffic to be preserved.

The principal arguments in favor of compulsory consolidation were the inequality of the earning power of the railroads, and the necessity for adequate transportation service over all roads. Something was said at the time in support of compulsory consolidation as to the economies that might be thereby accomplished, but the primary purpose was to so group the carriers that every section of the country having railroad facilities might have reasonably adequate service, and upon the same general level of rates.

While the Senate favored compulsory consolidation it proposed a trial period of seven years of voluntary consolidation under the supervision of the Commission.

In conference, the Senate compulsory feature was eliminated, but the Senate provision for investigation by the Commission into the subject matter of consolidation of the properties of common carriers into a limited

number of groups, which had been a part of the Senate compulsory plan, was retained.

The consolidation provisions of the Transportation Act are the result of a conference agreement, and authorize the Commission, after hearing all interested, to adopt a plan for the consolidation of all railroads subject to the Act to Regulate Commerce into a limited number of groups, and to publish the same. All consolidations are required to be in harmony with such plan as made, or as thereafter modified. The Transportation Act relieves all carriers effecting consolidations which are authorized or approved by the Commission, so far as may be necessary, from all prohibitions and restrictions of State and Federal laws in any wise prohibiting or limiting the right to consolidate. The Commission is directed, in preparing its grouping, to preserve competition as fully as possible and, whenever practicable, to preserve existing routes and channels of trade and commerce.

The Commission is further directed to so arrange the carriers in the several groups "that the cost of transportation as between competitive systems and as related to the values of the properties through which the service is rendered shall be the same, so far as practicable, so that these systems can employ uniform rates in the movement of competitive traffic, and under efficient management earn substantially the same rate of return upon the value of their respective railroad properties."

The Commission entered upon the investigation directed by Congress with reasonable promptness, presented a tentative plan grouping the carriers of the continental United States into 19 groups, and has been proceeding with due diligence, and probably will submit its report to Congress early in 1924.

Some of those who believe most strongly in consolidation, including some members of Congress, apparently regard the matter of grouping the carriers of the United States into consistent, logical, and self-sustaining groups, as an overnight job, and that the Commission, the

Railroads, or both, are responsible for undue delay in the grouping.

The carriers have, as a rule, and I believe without exception, endeavored to supply the Commission with all statistical and other information deemed by it necessary or desirable in the solution of the problem committed to it by the Transportation Act. The executives of the carriers appearing before the Commission have generally limited themselves to expressing their objections to the tentative grouping made by the Commission and to suggestions of other groupings, and have to only a limited extent discussed the feasibility or desirability of consolidations, or the possible harm resulting from impracticable or unwise grouping. This is primarily because the Commission has no jurisdiction over the question of whether or not there should be consolidations. Its inquiry is directed to the end of ascertaining the most logical basis of grouping under the mandate of Congress.

In the main, and if we assume no disturbance of the earning power of the roads included in any group by consolidation, the financial strength of any such group or of the carrier acquiring the properties constituting such group, must be a weighted average of the financial strength of the railroads constituting the group. It may be added that there is no process of dilution which does not weaken, and the financial strength of any group or carrier acquiring the properties constituting such group must be substantially less than that of the strongest carrier in the group.

However, no one can foretell what the final effect of coerced grouping may be upon the earning power of any group. The necessary result of compulsory consolidation will be to leave the earning power of the particular group so indefinite that it will have to demonstrate its capacity to earn in order to establish its credit.

On the other hand, if the process of consolidation and absorption is permitted to take an orderly course, to be worked out voluntarily along logical lines, the result will be properly developed systems of transportation,

with no serious financial results likely to follow such consolidations.

There are also grave constitutional doubts as to the power of Congress to compel one railroad corporation to buy or another to sell. In every such transaction, the value of the property of the selling carrier is involved. Necessarily, the value of such property is for judicial determination. That value cannot be fixed by Congress, nor can it be fixed by an administrative body, nor can Congress prescribe a rule by which such value may or must be determined.

Congress has not undertaken to deal with the basis of values to be employed in consolidations, except to provide that the par value of the stocks and bonds to be issued by the corporation which takes the ownership of the consolidated properties shall not exceed the aggregate value of such properties as found by the Interstate Commerce Commission under Section 19-a of the Valuation Act.

If Congress should decide upon compulsory consolidation it will have to solve many constitutional, legal, and practical problems of the gravest character, some of which are hereinafter set out in a comparison of the relative difficulties incident to compulsory consolidation in England and in the United States.

There seems to be a very strong conviction in the public mind, based upon assertion without any adequate consideration of the facts, that consolidations will make possible such great economies in operation as to permit a substantial reduction in rates without reducing net income. This is a very greatly exaggerated conception of the economies that may be effected as the result of consolidation. Some economies can be effected, but not sufficient to materially affect operating results; such economies, however, are likely to be more than offset by demands for the extension of the more elaborate service supplied on lines where the traffic justifies to lines where the traffic is not sufficient in quantity to compensate for the service now being rendered.

When the consolidation provisions of the Transportation Act were under consideration and the Senate was urging compulsory consolidation, and the House insisting upon voluntary consolidation when in the public interest and subject to the approval of the Interstate Commerce Commission, the Railway Executives declared in favor of a co-ordination of the carriers' lines, facilities and organizations and for the voluntary consolidation thereof under proper limitations, whenever in the public interest, to meet and provide for the reasonable demands of our domestic and foreign commerce.

The managing officers of The Atchison, Topeka and Santa Fe Railway Company recognize that Congress enacted the consolidation provisions of the Transportation Act in the belief that it was thereby materially aiding in the solution of the railroad problem.

It must also be conceded that members of Congress who favor compulsory consolidations believe such consolidations to be in the public interest, but they should realize that compulsory consolidation must inevitably impair the value of the securities, the earning power and credit of the stronger carriers, and their ability to adequately serve the patrons now dependent upon them for service. Their hope seems to be that the groups can be so arranged that each will have a reasonable assurance of earning a fair return upon the value of the property employed in that group in the transportation service.

The tentative grouping by the Interstate Commerce Commission includes as Santa Fe, System No. 16, The Atchison, Topeka and Santa Fe Railway System Lines, Denver and Rio Grande Western, Western Pacific, Colorado and Southern System, and Northwestern Pacific Railroad properties. The Atchison and Southern Pacific each own, exclusive of directors' qualifying shares, one-half the outstanding capital stock of the Northwestern Pacific Railroad Company, and such property is operated for alternate periods under a President selected by each of such companies, respectively. The Denver and Rio Grande Western and the Western Pacific are classed

as weak lines, while the Colorado and Southern System would probably not be classed as either a weak or strong line. The management of The Atchison, Topeka and Santa Fe Railway Company recommended the Commission permit the Northwestern Pacific to continue to be owned and operated as at present. No objection was interposed on behalf of the Atchison, Topeka and Santa Fe Railway Company to the proposed grouping by the Commission, its position being based upon an interpretation of the consolidation provisions of the Transportation Act, stated in the following language:

"In submitting the views of the management of The Atchison, Topeka and Santa Fe Railway Company and its affiliated carrier companies, and evidence in support thereof, it is assumed that in carrying out the plan of consolidation provided in the Transportation Act, no carrier is expected to part with its property for less than its actual value; that is, value ascertained on the basis of its net earning power, with due regard to the physical condition of such property and its adequacy as a transportation plant, and that no carrier is expected to pay more than such value for the property of any other carrier, regardless of what may have been the original cost, or the present cost of replacement thereof. It is further assumed that the requirements of the Transportation Act relating to the grouping of carriers are designed to effect a more economical and efficient transportation plant and service, and not to either burden or benefit the stockholders of one carrier to the advantage or disadvantage of the stockholders of another carrier."

In this connection it might be well to note that the basis of valuing the properties of the English railroads for the purpose of consolidation (there referred to as amalgamation), as prescribed by Parliament in the English Railways Act of August 19, 1921, is as follows:

"For the purpose of determining the terms and conditions of amalgamation between any constituent companies or of the transfer of the undertaking of any subsidiary company, the amalgamation tribunal

shall take into consideration all the circumstances of the case, and in particular the value on a net revenue earning basis of each of the constituent and subsidiary companies as a separate company, and its value as a component part of the amalgamated company; so, however, that regard shall not be had to economies or accretions of traffic or other circumstances tending to enhance its value as such component part attributable solely to the provisions of this Act relating to amalgamation and absorption."

It has been suggested that the apparent ease with which compulsory consolidation of the railroads of England, Scotland and Wales was accomplished demonstrates that there is no insuperable barrier, and perhaps no great difficulty, in a compulsory consolidation of the railroads of the United States into a limited number of groups. Those who have so concluded are evidently not familiar with the relative difficulties attendant upon compulsory consolidation in England and in the United States.

Parliament has, and exercised in the compulsory consolidation act, the supreme power, which cannot be challenged for want of constitutionality, of grouping the carriers of England, Scotland and Wales into regional groups, and conferred upon an administrative body, in case the carriers in any group failed to agree, the authority to determine the basis of amalgamation of the constituent companies, and the amount to be paid by the amalgamated companies for the property of the subsidiary companies in accordance with the above quoted provision of the Act of Parliament of August 9, 1921.

Here, Congress is met with the constitutional problem of compelling or inducing one railroad company to sell its private property, devoted to a public use, and of compelling or inducing another railroad company to buy such property, or of conferring upon one railroad company the authority to acquire by condemnation the private property of another railroad company devoted to a public use for the sole purpose of applying such private property when so acquired to the same public

use. It is not believed that Congress has the constitutional power to grant such authority.

In England railroad corporations are created by Parliament and railroad franchises are Parliamentary grants and there was not involved in the English consolidations the problem of dealing with corporations organized and exercising charter powers under the laws of forty-eight states, each of which imposes limitations upon the authority of corporations organized under its laws.

In England there was little or no necessity for unanimity of action by either bondholders or stockholders in effecting consolidation. Here, experience has demonstrated that in almost every effort to consolidate by agreement minority stockholders, sometimes having only nominal holdings, purchased for that purpose, challenge in legal proceedings the validity of every action taken looking to such consolidation. Such actions are quite frequently instituted for the purpose of compelling the purchase of such minority stock at an unconscionable price. The result, if nothing more, is much delay in effecting consolidation.

Here, the bonded indebtedness at par of many of the weaker carriers exceeds the actual value of the properties of such carriers. It is hardly possible that any plan of consolidation can be made effective without either a foreclosure sale, or if constitutionally and lawfully permissible, to condemn, without a condemnation proceeding. In England no such problem was involved.

Parliament in its grouping requirements, imposed by the English Railways Act of 1921, grouped all the railroads in England, Scotland and Wales into **four regional groups**, practically **eliminating competition**. Here, neither Congress nor the public has evidenced a desire, or even a willingness, to abandon or even to largely reduce, competition in service.

In England, the area of the country, the railroad mileage, and the diversity of interests, are much less than they are here. Without going into further detail, the conditions and problems here render compulsory consoli-

dation so much more difficult and the results so much more problematical than in England that no inferences as to the difficulties or effect of consolidations here can be drawn from consolidations there.

Voluntary consolidation, within reasonable limits, of control, management, operation and ownership of carrier properties, when in the public interest, under the supervision of the Interstate Commerce Commission, is the only form of consolidation that will bring practical and satisfactory results. It is particularly desirable that voluntary consolidations of constituent companies, composing existing system lines, should be proceeded with without delay. It is here that possible economies of consolidation will be most quickly and fully realized. Such system companies usually consist of a parent company and affiliated or subsidiary companies constructed or acquired in the logical and natural development of the channels of trade and commerce to and from the lines of the parent company.

That Congress has constitutional power to enlarge the corporate authority of railroad corporations organized under the laws of any one of the states and owning railroad properties engaged in interstate commerce so as to enable such corporations to effectively function as national transportation agencies, although this may involve consolidations, is believed by many able constitutional lawyers. It was apparently the purpose of Congress to accomplish this result by authorizing such consolidations when approved by the Interstate Commerce Commission, notwithstanding existing restrictions on or prohibitions of consolidations by law, state or national.

The validity of the exercise by state corporations of such authority in voluntary consolidations, if challenged by a State, can be determined without disturbing the credit or ability of any railroad company to properly discharge its functions and duties as a common carrier.

MSH #22835

**END OF
TITLE**